

TABLE OF CONTENTS

9.00 WILLFUL FAILURE TO COLLECT OR PAY OVER TAX

<u>9.01 STATUTORY LANGUAGE: 26 U.S.C. § 7202</u>	<u>9-1</u>
<u>9.02 GENERALLY</u>	<u>9-1</u>
<u>9.03 ELEMENTS</u>	<u>9-2</u>
9.03[1] Motor Fuel Excise Tax Prosecutions	9-5
<u>9.04 VENUE</u>	<u>9-6</u>
<u>9.05 STATUTE OF LIMITATIONS</u>	<u>9-6</u>

9.00 WILLFUL FAILURE TO COLLECT OR PAY OVER TAX

9.01 STATUTORY LANGUAGE: 26 U.S.C. § 7202

§7202. *Willful failure to collect or pay over tax*

Any person required under this title to collect, account for, and pay over any tax imposed by this title who willfully fails to collect or truthfully account for and pay over such tax shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined* not more than \$10,000, or imprisoned not more than five years, or both, together with the costs of prosecution.

* As to offenses committed after December 31, 1984, the Criminal Fine Enforcement Act of 1984 (P.L. 98-596) enacted 18 U.S.C. § 3623, which increased the maximum permissible fines for misdemeanors and felonies. Where 18 U.S.C. § 3623 **1** is applicable, the maximum fine under section 7202 for offenses committed after December 31, 1984, would be at least \$250,000 for individuals and \$500,000 for corporations. Alternatively, if any person derives pecuniary gain from the offense, or if the offense results in a pecuniary loss to a person other than the defendant, the defendant may be fined not more than the greater of twice the gross gain or twice the gross loss.

9.02 GENERALLY

This statute describes two offenses: (1) a willful failure to collect; and (2) a willful failure to truthfully account for and pay over. It was designed primarily to assure compliance by third parties obligated to collect excise taxes and to deduct from wages paid to employees the employees' share of Federal Insurance Contribution Act (FICA) taxes and the withholding tax on wages applicable to individual income taxes. The withheld sums are commonly referred to as "trust fund taxes." See *Slodov v. United States*, 436 U.S. 238, 242-48 (1978); *United States v. H.J.K. Theatre Corporation*, 236 F.2d 502 (2d Cir. 1956), *cert. denied*, 352 U.S. 969 (1957). The legislative history of the statute prior to 1975 is dis-

1 Changed to 18 U.S.C. § 3571, commencing November 1, 1986.

cussed in *United States v. Poll*, 521 F.2d 329, 333-34 n.2 (9th Cir. 1975). See also *United States v. Poll*, 538 F.2d 845 (9th Cir.), *cert. denied*, 429 U.S. 977 (1976).

9.03 *ELEMENTS*

To establish a violation of section 7202, the following elements must be proved beyond a reasonable doubt:

1. Duty to collect, and/or to truthfully account for and pay over;
2. Failure to collect, *or* truthfully account for and pay over; and
3. Willfulness.

Section 7202 has been seldom used, and there are few reported cases to use as a guide. Cases prosecuted under this statute usually involve the willful failure to truthfully account for and pay over social security taxes (FICA) and withholding tax. The duty of employers to truthfully account for and pay over is created by sections 3102(a), 3111(a), and 3402 of the Internal Revenue Code of 1986. See *United States v. Porth*, 426 F.2d 519, 522 (10th Cir.), *cert. denied*, 400 U.S. 824 (1970). Specifically, it is the individual with the duty to truthfully account for and pay over who is culpable when there is a failure to perform this duty. For an example of the criteria used to determine the individual with the duty to truthfully account for and pay over, see *Datlof v. United States*, 252 F. Supp. 11, 32 (E.D. Pa.), *aff'd*, 370 F.2d 655 (3d Cir. 1966), *cert. denied*, 387 U.S. 906 (1967), involving a civil penalty under 26 U.S.C. § 6672 for unpaid federal withholding and employment taxes.

The Tax Division's position historically has been that a willful failure truthfully to account for and pay over is a "breach of an inseparable dual obligation." *Manual for Criminal Tax Trials*, United States Department of Justice, Tax Division, Criminal Section, 5th Ed. 1973, p. 26. Under this theory, a willful failure to pay after a truthful accounting is made, by filing a return, would still leave "the duty as a whole unfulfilled and the responsible person subject to prosecution."

The requisite element of willfulness under section 7202 is the same as in other offenses under Title 26. *See* Section 8.06, *supra*. It must be shown that a defendant voluntarily and intentionally acted in violation of a known legal duty. *Cheek v. United States*, 498 U.S. 192 (1991); *United States v. Pomponio*, 429 U.S. 10, 12 (1976); *United States v. Bishop*, 412 U.S. 346, 360 (1973). Traditionally, however, this element has been difficult to establish in the context of a section 7202 prosecution.

The difficulty in proving willfulness resulted in the enactment of section 7215, a misdemeanor, for prosecution of "trust fund" cases. S. Rep. No. 1182, 85th Cong., 2d Sess. (1958), 2 U.S. Code Cong. & Ad. News 2187, 2189. The Senate Report on what became section 7215 commented on the criminal penalty provided for by section 7202, as follows:

This criminal penalty also has proved to be of limited usefulness because of the difficulty of proving willfulness, which to a lesser extent has also been a problem in the case of the civil penalty. The courts, for example, in the criminal cases generally have refused to treat as "willful" those cases where the employer failed to pay over amounts withheld because they used the funds in business ventures which were not successful and no longer had such amounts available to be paid over to the Government.

The difficulty in the approach taken by the courts is illustrated by *United States v. Poll*, 521 F.2d 329 (9th Cir. 1975). In *Poll*, the parties stipulated that the amount of taxes which should have been withheld was correctly shown on the corporate books but that the defendant knowingly signed and filed false returns (Forms 941), which did not correctly reflect the amount withheld from wages. In reversing the conviction, the Ninth Circuit held that to establish a willful failure to truthfully account for and pay over taxes required to be withheld, both the failure to truthfully account for and the failure to pay over must be willful. As the Ninth Circuit viewed it, in addition to establishing a willful failure to truthfully account for taxes required to be withheld:

[t]he Government must establish beyond a reasonable doubt that at the time payment was due the taxpayer possessed sufficient

funds to enable him to meet his obligation or that the lack of sufficient funds on such date was created by (or was the result of) a voluntary and intentional act without justification in view of all the financial circumstances of the taxpayer.

Poll, 521 F.2d at 333.

The *Poll* court also concluded that it was error not to allow the defendant to introduce evidence that the corporation lacked the money to pay the full amount of the taxes and that the defendant intended to make up the deficiencies later. This view ignores the fact that the duty imposed is not simply the duty to pay taxes, but also includes the duty to truthfully account for taxes, and that defendant Poll admittedly filed false returns. Contrary to the *Poll* decision, an inability to pay does not excuse the duty to truthfully account for the taxes that are due. ²

Poll is incorrectly decided. However, where there is a willful failure to truthfully account for withheld taxes and some additional burden is imposed by the court, as suggested by *Poll*, the government can meet that burden with testimony by employees or suppliers that other creditors were paid during the period in question and that any lack of funds to pay was voluntary and intentional.

It should be noted that Poll did not go free. Following the reversal of his conviction, the government promptly secured a new indictment that did not charge him with a section 7202 violation, but with filing a false return in violation of section 7206(1). His conviction was affirmed on appeal. *United States v. Poll*, 538 F.2d 845 (9th Cir.), *cert. denied*,

² For cases holding that in a prosecution under 26 U.S.C. § 7203, the government need not prove that at the time the defendant filed his returns, he possessed readily available funds with which to pay his taxes, see *United States v. Ausmus*, 774 F.2d 722, 725 (6th Cir. 1985), and *United States v. Tucker*, 686 F.2d 230, 233 (5th Cir. 1982). *Ausmus* and *Tucker* rejected *United States v. Andros*, 484 F.2d 531, 533-34 (9th Cir. 1973), a case in which the Ninth Circuit stated, in dicta, that to establish a willful failure to pay under section 7203, the government must prove that the taxpayer possessed sufficient funds to meet his tax obligations and that the taxpayer voluntarily and intentionally did not pay the tax due.

July 1994

FAILURE TO COLLECT/PAY

429 U.S. 977 (1976). For a successful conviction under section 7202, *see United States v. Scharf*, 558 F.2d 498 (8th Cir. 1977), where the court held that evidence that the defendant had altered records was admissible for the purpose of showing, "motive, intent, and willfulness." *Scharf*, 558 F.2d at 501. For a case in which the court had no difficulty in concluding that defendant's conduct was willful in a section 7202 prosecution, *see United States v. Bailey*, 789 F. Supp. 788, 814 (N.D. Tex. 1992) (failure to pay over taxes withheld from employees' paychecks for almost a decade found to be willful).

9.03[1] *Motor Fuel Excise Tax Prosecutions*

Care must be exercised to insure that section 7202 is not applied to those who have the duty to pay the tax at issue. Section 7202 applies to a person who is not the taxpayer but is under a duty to collect the tax from the taxpayer and then to truthfully account for the collected tax to the government and pay it over. Often, the one responsible for the tax will pass it on to another, as, for example, by including it as part of the price of goods. But the fact that the taxpayer "collects" the tax from another in this sense does not mean that he is responsible under the law for collecting the tax and, thus, potentially subject to prosecution under section 7202.

Consequently, it is the position of the Department of Justice that section 7202 charges are not appropriate in a motor fuel excise tax case. There is no obligation, within the meaning of section 7202, to collect and pay over these gasoline taxes. *See United States v. Musacchia*, 955 F.2d 3 (2d Cir. 1991) (vacating defendant's conviction under section 7202 after being advised by Department of Justice that section 7202 "does not apply to the gasoline taxes at issue here"). *Musacchia*, 955 F.2d at 4.

9.04 *VENUE*

If a statute does not indicate where Congress considers the place of committing a crime to be, "the *locus delicti* must be determined from the nature of the crime alleged and

the location of the act or acts constituting it." *United States v. Anderson*, 328 U.S. 699, 703 (1946). Although no venue cases have been found, venue would appear to be proper in a section 7202 prosecution in the judicial district in which the defendant was required to collect or pay over the tax.

For a general discussion of venue, *see* Section 6.00, *supra*.

9.05 STATUTE OF LIMITATIONS

The statute of limitations for prosecutions under section 7202 is six years. *See United States v. Musacchia*, 900 F.2d 493, 499-500 (2d Cir. 1990), *vacated in part on other grounds*, 955 F.2d 3, 4 (2d Cir.), *cert. denied*, 111 S. Ct. 2887 (1991); *United States v. Porth*, 426 F.2d 519, 522 (10th Cir.), *cert. denied*, 400 U.S. 824 (1970). Be aware, however, that one district court to consider the question has concluded that the statute of limitations for section 7202 prosecutions is three years. *United States v. Block*, 497 F. Supp. 629, 630-32 (N.D. Ga. 1980), *aff.d* 660 F.2d 1086 (5th Cir. 1980).

In the *Block* court's view, the omission of the language "collect, account for, and pay over" from the subsections of 26 U.S.C. § 6531, which establish the longer six-year period of limitations, demonstrates that Congress did not intend to make the failure to "pay over" third party taxes subject to the six-year statute of limitations. *Block*, 497 F. Supp. at 630-32.

The court also noted in *Block*, 497 F. Supp. at 632, that section 6531(4) was not directed at a class of offenses but rather to "the offense of willfully failing to pay any tax." The court reasoned that it was "quite clear" that failure to pay over third-party taxes was substantively different from a failure to pay taxes; thus, the exception contained in section 6531(4) was found not to apply to the failure to pay over third-party taxes. *But see Wilson v. United States*, 250 F. 2d 312, 320 (9th Cir. 1958).

The Second Circuit, in *Musacchia*, reviewed the *Block* decision and concluded that that "court's analysis is not convincing." *Musacchia*, 900 F.2d at 499-500. The *Musacchia* court

July 1994

FAILURE TO COLLECT/PAY

found that although 26 U.S.C. § 6531(4) does not track the language of section 7202 exactly, the terms "pay" and "pay over" were used interchangeably by the Supreme Court in deciding *Slodov v. United States*, 436 U.S. 238, 249 (1978), and thus the fact that section 6531(4) uses the term "pay" rather than "pay over" is not dispositive.

Instead, the *Musacchia* court found persuasive the government's argument that "it would be inconsistent for Congress to have prescribed a six-year limitations period for the misdemeanor offense defined in 26 U.S.C. § 7203 . . . while providing only a three-year limitation period for the felony offense defined in Section 7202." *Musacchia*, 900 F.2d at 500. The court also noted that the language of section 6531(4) supports the conclusion that the six-year limitations period applies in a section 7202 prosecution. *Musacchia*, 900 F.2d at 500.

The Tax Division takes the position that *Porth* and *Musacchia* are correctly decided and that the six-year statute of limitations provided for in section 6531(4) is applicable to prosecutions under section 7202.